

145705

DEPT. OF TRANSPORTATION
DOCKETS
01 DEC 21 PM 2:49

BEFORE THE
DEPARTMENT OF TRANSPORTATION
WASHINGTON, D.C.

U.S.-U.K. Alliance Case

:
:
:

Docket OST-2001-11029 -54

REPLY OF FEDERAL EXPRESS CORPORATION

Communications with respect to this document should be sent to:

M. Rush O'Keefe, Jr.
Vice President-Regulatory Affairs
Sarah S. Prosser
Managing Director
FEDERAL EXPRESS CORPORATION
3620 Hacks Cross Road
Building B, 3rd Floor
Memphis, Tennessee 38125

Nancy S. Sparks
Managing Director
FEDERAL EXPRESS CORPORATION
1101 Pennsylvania Avenue, N.W., Suite 600
Washington, D.C. 20004
(202) 756-2461 (voice)
(202) 756-7540 (fax)
E-Mail: nssparks@fedex.com

Attorneys for
FEDERAL EXPRESS CORPORATION

December 21, 2001

BEFORE THE
DEPARTMENT OF TRANSPORTATION
WASHINGTON, D.C.

U.S.-U.K. Alliance Case

:
:
:

Docket OST-2001-11029

REPLY OF FEDERAL EXPRESS CORPORATION

The comments and answers filed in opposition to the proposed transactions suffer from a fundamental misconception of the issues before the Department in this proceeding. They essentially argue a hypothetical question, *i.e.*, whether the transactions are in the public interest under a *de facto* and *de jure* open skies regime. Unfortunately, that is not the issue before the Department.

The issue before the Department is whether approval of the transactions, including the grant of antitrust immunity, together with an open skies regime not otherwise obtainable for the United States, is in the public interest.

In order to make that determination, the Department must first assess the benefits of an open skies regime. In light of the well-recognized problems of achieving *de facto* open entry at Heathrow, the Department should begin its analysis by assessing the benefits of open skies in all other contexts. Those include the immensely valuable benefits to be obtained from open skies

December 21, 2001

for all-cargo transportation, as well as the benefits of open skies on operations of other airports such as Gatwick. For example, it is of no benefit to the Department to assess (as the Department of Justice does) Gatwick as a competitive alternative under Bermuda 2's rules as opposed to assessing Gatwick as a competitive alternative under an open skies regime. Only after these analyses are completed can the Department determine what remedies are required, if any, to ensure that the approval of the transaction is in the public interest. Here again, the test is not what remedies are required to achieve a hypothetically *de facto* open entry regime at Heathrow, because that may well be impossible. Even the United States has capacity-constrained airports. Rather, the appropriate test for the Department is what remedies, when applied to Heathrow, create public benefits which, when quantified and added to the other public interest benefits, outweigh any potential adverse effect on the public interest. That is the test before the Department.

FedEx is particularly concerned that none of the parties, including the Department of Justice, have fully addressed the immensely valuable benefits of open skies to U.S. shippers and exporters.¹ An open skies agreement will reduce costs and increase flexibility for U.S. shippers by removing regulatory impediments to efficient air express/cargo routings. As previously discussed, all-cargo operators require open fifth-freedom rights, broad route flexibility, and


¹ Continental's answer for example is misleading, in that it states that "[t]he only benefit" will be opening access to Heathrow and Gatwick. Answer and Supplemental Comments of Continental at 20 (Dec. 17, 2001).

unrestricted change-of-gauge rights to construct the most economical routing for their aircraft. These rights would enable them to maximize aircraft usage and minimize aircraft movements. The enclosed statement of Frederick W. Smith, Chairman, President and CEO of FedEx Corporation, before the Senate Judiciary Committee discusses the importance of open skies to U.S. shippers and exporters. Exhibit 1. These benefits are also fully described in our November 2, 2001 answer to the American Airlines/British Airways applications at pages 9-10 (including exhibits), and in our November 9, 2001 reply in that docket at pages 2-3 and note 2.

More efficient air express/cargo service between the United States and the United Kingdom would generate benefits and create jobs in all sectors of the U.S. economy.² Open skies agreements with other countries have created U.S. jobs because U.S. exporters gained access to the highest quality and lowest cost air express/cargo networks that distribute U.S.-manufactured products in foreign markets. In addition, U.S. businesses rely on global air express networks to decrease their expenses and to increase their efficiency by using just-in-time inventory management programs. In total, the absence of open skies means that U.S. businesses cannot operate at their optimal levels.

² Reply of Federal Express Corporation to Joint Applications, 2001-10387-134 at 2 (November 9, 2001).

Accordingly, Federal Express urges the Department to act quickly on the applications for antitrust immunity to ensure that the U.S. economy always enjoys the economic benefits that would be derived from a comprehensive U.S.-U.K. open skies agreement. In so doing, it should give full consideration to the value of expanded all-cargo rights between the United States and the United Kingdom.



Nancy S. Sparks
Managing Director
FedEx Express

Statement for the Senate Judiciary Committee
Regarding the American Airlines/British Airways Alliance

Frederick W. Smith
Chairman, President and CEO
FedEx Corporation

I appreciate the opportunity offer this statement on behalf of FedEx Corporation and its subsidiary, FedEx Express, about the proposed alliance of British Airways and American Airlines. At the present time, FedEx's interest in this alliance is primarily focused on its unbreakable link to the reform of one of the U.S.'s oldest air services agreement, the 1978 agreement with the U.K. Commonly known as "Bermuda II," this agreement remains one of the most outmoded aviation agreements to which the U.S. is a party. In order to understand where we are today, it might be helpful to see this agreement in its historic context.

It begins in 1994, in the midst of World War II. The venerable DC-3 is the mainstay of the U.S. airline industry. The first military jet aircraft have only recently taken to the skies, and the inaugural flights of the first commercially successful jet aircraft – the DC-8 and the 707 - are still 15 years away. This is what the world looked like when delegates met in Chicago to develop a framework for facilitating international passenger transportation.

It should come as no surprise then that the 1944 Chicago Convention, and the subsequent bilateral agreements framed by national governments to facilitate point-to-point passenger transportation, continue to inhibit the development of efficient, world-wide, hub-and-spoke networks utilized today by all-cargo carriers for the rapid movement of high-value goods. The Convention's framers could never have dreamed that one day hundreds of wide-bodied jets would crisscross the skies each day, carrying millions of tons of cargo over thousands of miles.

Bermuda II continues these types of restrictions, allowing bilateral services but hamstringing today's all cargo networks with its restrictions on traffic rights beyond the U.K. For all-cargo services unlike for combination, the transatlantic

rights were liberalized in 1980, but the restrictions on U.S. third-country traffic rights that impact today's cargo network remain to this day.

Meanwhile, on April 17, 1973, however, Federal Express revolutionized all-cargo services by introducing the first integrated air/ground express operations. On that first night, our 389 employees delivered 186 packages to 25 U.S. cities using 14 Falcon jets. Today, FedEx Express is one of six independent operating companies that make up FedEx Corporation. Collectively, our more than 215,000 employees and contractors deliver nearly 5 million shipments every business day to 211 countries. We operate 662 aircraft, the largest all-cargo fleet in the world and second largest overall. In 24 hours, those aircraft travel more than 450,000 miles, a distance of about 17 trips around the equator.

As a leader in the aviation industry, it might be useful to examine what has allowed FedEx to grow from 186 packages a night to 5 million, or from 14 aircraft to 662, or from 389 employees to more than 215,000 employees and contractors. The answer is in two parts.

First, we have followed the advice enunciated by Walt Kelly's great comic strip character, Pogo: "If you want to be a great leader, find a big parade and run in front of it." Since its inception, our company and our industry have been doing exactly that. We have been running in front of the parade of four powerful trends shaping the world economy: (1) the increase in high-tech and high-value-added products as a percentage of all economic activity; (2) globalization; (3) fast-cycle logistics; and (4) electronic commerce.

The second, and equally important, part of the answer to the question of FedEx's phenomenal growth is deregulation. Had the U.S. Congress not had the good sense and foresight to deregulate both domestic aviation and trucking, the express industry would never have grown to be the engine of world trade that it is today. More importantly, the U.S. economy would have been deprived of the benefits provided by our industry. For example, in 1977, prior to deregulation, the United States spent approximately 17% of its GDP on logistics. Today, that figure has fallen to 10%. That seven percentage points of GDP productivity increase since 1977 undoubtedly contributed to all of the social improvements this country has enjoyed over those 25-odd years, including improved Medicare and Social Security benefits. Absent deregulation, those improvements would not and could not have taken place.

As a direct result of the United States' successful Open Skies policy, much progress has also been made over the past decade in the struggle to achieve similar deregulation of international air cargo transportation. Indeed, the U.S. has now negotiated more than fifty Open Skies agreements in every region of the world. The U.S.-U.K. agreement remains an unfortunate exception to that trend.

Today, more than 50 years after the Chicago Convention, global aviation has undergone a radical transformation, yet the ability of U.S. all-cargo carriers to respond to the needs of shippers and consumers continues to be hampered by restrictive bilaterals such as the Bermuda II agreement. Its restrictions on beyond traffic rights, change of gauge and routing flexibility makes it a formidable obstacle to the efficient operation of US express operations serving the U.K.

Reviewing that “big parade”: those same four macroeconomic forces - (1) high-tech and high-value-added products, (2) globalization, (3) fast-cycle logistics, and (4) electronic commerce – keep marching along. While goods moved by air account for less than 2% of all tonnage moved in international trade, they now represent over 40% of its value. As recently as 1970, international trade accounted for only 10% of U.S. GDP. In 2000, it was approximately 25%. That means about a quarter of every dollar produced by our economy is now related to international trade, and this figure will increase in coming years. McKenzie and Company estimates that today, a little over 20% of all manufactured goods are moved across borders, but by 2025, that number may be in excess of 80%.

The current aviation bilateral system, originally designed for point-to-point passenger operations, continues to be used as a sword-and-shield by the U.K. government on behalf of its carriers to resist meeting true market demands in the express and cargo markets. This forces both U.S. and U.K. exporters and importers of goods by air to accept less efficient, less desirable services. Numerous independent studies around the world have verified this finding in economies with restrictive international aviation regimes.

We at FedEx strongly believe that all-cargo services are commerce-enablers and should be fully and fairly liberalized, whether in conjunction with or separately from combination services. In that regard, we applaud the U.S. Government's successful efforts to include 7th freedom rights for all-cargo carriers in its recent Open Skies bilaterals such as the recent agreement with France.

It is important to remember that the cargo business is not bilateral in nature, so the very foundation of a bilateral aviation treaty is at odds with the flow of goods around the world. In the same vein, the 5th and 6th freedom rights should be treated exactly the same, which was the original interpretation in the 1944 Chicago Conference. Because this has not been the case, British carriers now enjoy a competitive advantage over U.S. carriers based purely on the geography of their home countries. Accordingly, we urge the U.S. Government, in negotiating with countries around the world, to require as a matter of course direct equality of 6th freedom rights to 5th freedom rights, at least as applied to all-cargo operations. This can best be achieved by an open skies agreement with no limitation on fifth freedom operations.

The U.S. Government must also strive to ensure that rights granted U.S. carriers under our bilaterals, including our Open Skies agreements, are fully useable. U.S. carriers are increasingly confronted with capacity and environmental restrictions at airports around the world. These *de facto* restrictions on our operations often effectively trump our *de jure* rights under the bilaterals.


Some passenger carriers have attempted to use this concept of “fully-useable rights to insist that an agreement with the United Kingdom that does not fulfill all their desires for slots at London’s Heathrow Airport does not achieve true liberalization. It is important for this Committee to understand that Heathrow is one of three London airports. While it is historically prized by combination carriers for its status as a connecting airport, that role is being significantly challenged by the growth of powerful alliance hubs on the European continent. We should not let the issue of access to a single airport stop the effort for open skies in this long-restricted market. Instead we should be pressing our European and British counterparts to reform the slot trading system in Europe, so that U.S. and other carriers seeking access to a slot-restricted airport can in fact use self-help to gain access rather than continuing to rely on governmental intervention. Also, we should continue to urge an increase in capacity as well as the most effective use of that capacity at British airports.

FedEx has been actively advocating this position in the U.S. Department of Transportation proceedings on the alliance, a position that FedEx has put forward for at least ten years of debate over U.S.-U.K. open skies. This is a great opportunity to move forward toward open opportunities for all carriers in the

important transatlantic corridor linking the U.S. and the U.K. We should not let it slip away.

CERTIFICATE OF SERVICE

I hereby certify that I have this 21st day of December 2001, mailed, postage prepaid, true copies of the foregoing Reply of Federal Express Corporation to the following:



R. Bruce Keiner, Jr.
Lorraine B. Halloway
Thomas Newton Bolling
Crowell & Moring LLP
1001 Pennsylvania Ave., N.W.
10th Floor North
Washington, D.C. 20004-2595

Robert E. Cohn
Alexander Van der Bellen
Shaw Pittman LLP
2300 N Street, N.W.
Washington, D.C. 20037

Andrea Fischer Newman
Senior Vice President, Government
Affairs
David G. Mishkin
Vice President, International &
Regulatory Affairs
Megan Rae Rosia
Managing Director, Government
Affairs & Associate General
Counsel
Northwest Airlines, Inc.
901 15th Street, N.W.
Suite 310
Washington, D.C. 20005

Jeffrey A. Manley
Wilmer, Cutler & Pickering
2445 M Street, N.W.
Washington, D.C. 20037

Michael F. Goldman
Silverberg, Goldman & Bikoff
1101 30th Street, N.W.
Suite 120
Washington, D.C. 20007

Roger W. Fones
Chief, Transportation, Energy &
Agriculture Section
Antitrust Division
Department of Justice
325 7th Street, N.W.
Washington, D.C. 20520

David L. Vaughan
Kelley Drye & Warren LLP
1200 19th Street, N.W.
Suite 500
Washington, D.C. 20036

Stephen H. Lachter
1150 Connecticut Ave., N.W.
Suite 900
Washington, D.C. 2003

Marshall S. Sinick
Squire, Sanders & Dempsey,
1201 Pennsylvania Ave., N.W.
Suite 500
Washington, D.C. 20004

Nathaniel P. Breed, Jr.
Shaw Pittman
2300 N Street, N.W.
Washington, D.C. 20037

Joel Stephen Burton
Donald T. Bliss
Patrick R. Rizzi
O'Melveny & Myers LLP
555 13th Street, N.W.
Suite 500 West
Washington, D.C. 20004

Richard P. Taylor
Steptoe & Johnson LLP
1330 Connecticut Ave., N.W.
Washington, D.C. 20036

Office of Aviation Negotiations
Department of State
2201 C Street, N.W.
Room 5531
Washington, D.C. 20520

Edgar N. James
Marie Chopra
James & Hoffman, P.C.
1101 17th Street, N.W.
Suite 510
Washington, D.C. 20036

John L. Richardson
Crispin & Brenner, P.L.L.C.
1156 15th Street, N.W.
Suite 1105
Washington, D.C. 20005

James Fry
Manager, Contracts &
Regulatory Affairs
World Airways, Inc.
HLH Building, 101 World Drive
Peachtree City, GA 30269

Brian T. Hunt
American Trans Air
P.O. Box 51609
Indianapolis, IN 46251

Joanne W. Young
Baker & Hostetler LLP
1050 Connecticut Ave., N.W.
Suite 1100
Washington, D.C. 20005

Jeffrey N. Shane
Hogan & Hartson L.L.P.
555 13th Street, N.W.
Washington, D.C. 20004

William C. Evans
Verner, Liipfert, Bernhard,
McPherson and Hand
901 15th Street, N.W.
Suite 700
Washington, D.C. 20005

Alfred J. Eichenlaub
Vice President & General Counsel
Polar Air Cargo, Inc.
100 Oceangate
15th Floor
Long Beach, CA 90802

U.S. Transcom/TCJS
Attention: Air Mobility
508 Scott Drive
Scott AFB, IL 62225

James W. Tello, Esq.
P.O. Box 66824
Washington Square Station
Washington, D.C. 20035

First Secretary (Transport)
British Embassy
3100 Massachusetts Ave., N.W.
Washington, D.C. 20008

Robert D. Papkin
Squire, Sanders & Dempsey, LLP
1201 Pennsylvania Ave., N.W.
Suite 500
Washington, D.C. 20004

Donald C. Comlish
7504 Heatherton Lane
Potomac, MD 20854

Daryl Libow
Sullivan & Cromwell
1701 Pennsylvania Avenue, N.W.
Suite 800
Washington, D.C. 20006

Burton J. Rubin
General Counsel
Paul M. Ruden
Senior Vice President
American Society of Travel Agents,
Inc.
110 King Street
Alexandria, VA 22314

Carl B. Nelson, Jr.
Associate General Counsel
Greg A. Sivinski, Senior Attorney
American Airlines, Inc.
1101 17th Street, N.W., Suite 600
Washington, D.C. 20036

Don H. Hainbach
Boros & Garofalo
1201 Connecticut Avenue, N.W.
Suite 500
Washington, D.C. 20004

D. Scott Yohe
Senior Vice President - Government
Affairs
Delta Air Lines, Inc.
1275 K Street, N.W., Suite 1200
Washington, D.C. 20005

William Evans
Verner Liipfert Bernhard McPherson
And Hand, Chartered
901 15th Street, N.W., #700
Washington, D.C. 20005

Mark C. Schechter
Howrey Simon Arnold & White LLP
1229 Pennsylvania Avenue, N.W.
Washington, D.C. 20004

Ava L. Mims
Deputy Director, AFS-2
Federal Aviation Administration
800 Independence Avenue, S.W.
Washington, D.C. 20591

John Wood
Executive Vice President
External Affairs, Americas
British Airways Plc
1850 K Street, N.W., #300
Washington, D.C. 20006

Paul C. Jasinski
General Counsel, Americas
James B. Blaney
Senior Counsel, Americas
British Airways Plc
75-20 Astoria Boulevard
Jackson Heights, New York 11370

Henry C. Joyner
Senior Vice President - Planning
American Airlines, Inc.
P.O. Box 619616, MD 5628
DFW Airport, Texas 75261

C. David Cush
Vice President - International
Affairs and Alliances
American Airlines, Inc.
P.O. Box 619616, MD 5635
DFW Airport, Texas 75261

William K. Ris, Jr.
Senior Vice President -
Government Affairs
American Airlines, Inc.
1101 17th Street, N.W.
Suite 600
Washington, D.C. 20036

J. Otto Grunow
Managing Director -
International Affairs
American Airlines, Inc.
P.O. Box 691616, MD 5639
DFW Airport, Texas 75261

John J. Varley
Assistant General Counsel
Delta Air Lines, Inc.
Law Department (#981)
1030 Delta Boulevard
Atlanta, Georgia 30320-2574

Rebecca G. Cox
Vice President, Government Affairs
Continental Airlines, Inc.
1350 I Street, N.W.
Washington, D.C. 20005

Hershel I. Kamen
Staff Vice President, International &
Regulatory Affairs
Continental Airlines, Inc.
P.O. Box 4607 - HQSGV
Houston, Texas 77210-4607

Barry K. Humphreys
Director, External Affairs &
Route Development
Hugh M. Ford
General Manager, Legal
Virgin Atlantic Airways Limited
The Office, Manor Royal
Crawley, West Sussex
RH10 2NU United Kingdom

Richard M. Vacar
Director
Hoyt L. Brown
Deputy Director
Department of Aviation
City of Houston
16930 John F. Kennedy Boulevard
Houston, Texas 77032

Miguel R. San Juan
President, World Trade Division
Greater Houston Partnership
1200 Smith Street, Suite 700
Houston, Texas 77002

Rebecca L. Taylor
Nicholas S. Penn
Leftwich & Douglas, P.L.L.C.
1401 New York Avenue, N.W.
Washington, D.C. 20005-3922

Edward P. Faberman
Michelle M. Faust
Air Carrier Association of America
1500 K Street, N.W., Suite 250
Washington, D.C. 20005-1714

Lawrence M. Nagin
Executive Vice President - Corporate
Affairs & General Counsel
Rachel Teipe
Senior Counsel
U.S. Airways, Inc.
Crystal Park Four
2345 Crystal Drive
Arlington, Virginia 22227

Kevin E. Cox
Senior Executive Vice President
American Airlines, Inc.
DFW International Airport
P.O. Drawer DFW
DFW, Texas 75261

Daniel M. Kasper
LECG, LLC
350 Massachusetts Avenue
Suite 30
Cambridge, Massachusetts 02139

Elliott M. Seiden
Garfinkle & Wang PLC
1555 Wilson Boulevard
Suite 301
Arlington, Virginia 22209